

Internal Revenue Service
Director, Exempt Organizations

Department of the Treasury
P.O. Box 2508 - EODQA Rm. 7008
Cincinnati, OH 45201

Date: OCT 09 2003

Employer Identification Number: [REDACTED]

Person to Contact - I.D. Number: [REDACTED]

Contact Telephone Numbers: [REDACTED]

Dear Sir or Madam:

We have considered your application for recognition of exemption from Federal income tax under the provisions of section 501(c)(3) of the Internal Revenue Code of 1986 and its applicable Income Tax Regulations. Based on the available information, we have determined that you do not qualify for the reasons set forth on Enclosure I.

Consideration was given to whether you qualify for exemption under other subsections of section 501(c) of the Code. However, we have concluded that you do not qualify under another subsection.

As your organization has not established exemption from Federal income tax, it will be necessary for you to file an annual income tax return on Form 1120 because you are an unincorporated association. Contributions to you are not deductible under section 170 of the Code.

If you are in agreement with our proposed denial, please sign and return one copy of the enclosed Form 6018, Consent to Proposed Adverse Action.

You have the right to protest this proposed determination if you believe it is incorrect. To protest, you should submit a written appeal giving the facts, law and other information to support your position as explained in the enclosed Publication 892, "Exempt Organizations Appeal Procedures for Unagreed Issues." The appeal must be submitted within 30 days from the date of this letter and must be signed by one of your principal officers. You may request a hearing with a member of the office of the Regional Director of Appeals when you file your appeal. If a hearing is requested, you will be contacted to arrange a date for it. The hearing may be held at the Regional Office or, if you request, at any mutually convenient District Office. If you are to be represented by someone who is not one of your principal officers, he or she must file a proper power of attorney and otherwise qualify under our Conference and Practice Requirements as set forth in Section 601.502 of the Statement of Procedural Rules. See Treasury Department Circular No. 230.

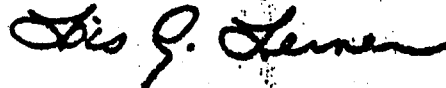
If you do not protest this proposed determination in a timely manner, it will be considered by the Internal Revenue Service as a failure to exhaust available administrative remedies. Section 7428(b)(2) of the Internal Revenue Code provides, in part, that:

A declaratory judgment or decree under this section shall not be issued in any proceeding unless the Tax Court, the Claims Court, or the district court of the United States for the District of Columbia determines that the organization involved has exhausted administrative remedies available to it within the Internal Revenue Service.

We have sent a copy of this letter to your representative as indicated in your power of attorney.

If we do not hear from you within the time specified, this will become our final determination. In that event, appropriate State officials will be notified of this action in accordance with the provisions of section 6104(c) of the Code.

Sincerely,



Lois G. Lerner
Director, Exempt Organizations
Rulings and Agreements

Enclosures:

Enclosure :
Form 6019
Publication 992

Enclosure I

Facts:

Your application indicates that you were formed for the purpose of composing, producing and presenting [REDACTED] for the educational benefit of those selected to play these compositions [REDACTED]. In addition, compositions may be recorded and produced for the benefit of the founder, who also calls himself the owner.

The application also listed several "officers" who will be compensated on a "pay-for-play" basis as musicians only if they participate in the activities of the organization. They do not have any administrative power with the organization. The "board members" are personally selected by [REDACTED] who has sole control as to the amount of compensation the musicians receive and the tenure that each has with the organization.

Your application was initially submitted without any kind of written governing document. On March 22, 2003, a "constitution" was adopted. The Constitution includes (but is not limited to) the following provisions:

- a. The purpose of the organization is to guarantee total promotion of this group of musicians and vocalists formed by the founder to gain success individually and as a group through the production of musical compositions and the potential release of such compositions to the country.
- b. Article III states that the power of the founder/owner is absolute. It also states that this person is the officer of power in charge and that he has full and total responsibility of all financial and compensation issues. [REDACTED]
- c. Article IV states that all compositions will ultimately be the [REDACTED], which is solely controlled by the founder/owner. This Article also states that it is hoped that one day a record company will sign the group to a recording contract. Once the product is being distributed to the general public, the stated goal and objective of the organization is to obtain professional and musical independence.
- d. Article V, section 6, states that the founder has the power to distribute reasonable compensation in furtherance of its purposes. Section 7 states that the organization itself will not have any gross or net income, and thus not purchase any assets for the organization itself, and therefore there will be no assets to distribute at time of dissolution. However, any

currently held assets would continue to be held by the founder if the organization were to dissolve.

Your application states that the final recorded product may possibly produced for the sale and distribution to the general public. The musical sessions take place in the home of the founder, and the recordings are composed and conducted completely by the founder.

Per page two, part II, item two of your application, 100% of the organization's support has come [REDACTED]. It was stated that an application to receive a grant has been filed with [REDACTED] to further your activities and that the receipt of this grant is based on whether your organization receives exemption under section 501(c)(3) of the Code. However, [REDACTED] as stated that this grant has been applied for in his name and not the organization, as he is to be responsible for all financial transactions.

In general, information in the original application and subsequent correspondence indicates that this organization is the [REDACTED] and was formed to enable him to receive grant funding that is only available to 501(c)(3) organizations, in order to further [REDACTED] [REDACTED] has total operational, artistic, and financial control over the organization. Other "officers" are involved only as [REDACTED] and working under [REDACTED] direction.

Law:

Section 501(c)(3) of the Code provides for the exemption from federal income tax of organizations organized and operated exclusively for educational purposes.

Section 1.501(c)(3)-1(d)(3)(i) of the regulations provides that the term "educational", as used in section 501(c)(3), relates to-

- (a) The instruction or training of the individual for the purpose of improving or developing his capabilities; or
- (b) The instruction of the public on subjects useful to the individual and beneficial to the community.

Section 1.501(c)(3)-1(a)(1) of the Income Tax Regulations states that, in order to be exempt as an organization described in section 501(c)(3) of the Code, an organization must be both organized and operated exclusively for one or more of the purposes specified in such section. If an organization fails to meet either the organizational test or the operational test, it is not exempt.

Section 1.501(c)(3)-1(c)(1) of the regulations provides that an organization will be regarded as "operated exclusively" for one or more exempt purposes only if it engages primarily in activities which

accomplish one or more of such exempt purposes specified in section 501(c)(3). An organization will not be so regarded if more than an insubstantial part of its activities is not in furtherance of an exempt purpose.

Section 1.501(c)(3)-1(d)(1)(ii) of the regulations states that an organization is not organized or operated exclusively for one or more exempt purposes unless it serves a public rather than a private interest. Thus, to meet the requirement of this subdivision, it is necessary for an organization to establish that it is not organized or operated for the benefit of private interests such as designated individuals, the creator or his family, shareholders of the organization, or persons controlled, directly or indirectly, by such private interests.

Revenue Ruling 65-271, 1965-2 CB 161, an organization focused on stimulating interest in jazz, and has paid professional jazz musicians. Its specific activities include conducting public festivals and traveling to public high schools where members of the community are encouraged to participate. Musicians from the community are encouraged to present new works. All activities described are for public benefit as they give the community an opportunity to take part. This organization received exemption under section 501(c)(3) of the Code, as they are serving an educational purpose as a cultural organization to the general public.

Revenue Ruling 69-175, 1969-1 CB 149, when a group of individuals associate to provide a service for themselves, they are serving a private interest. Thus, an organization operating in a similar fashion would not be exempt from Federal income tax under section 501(c)(3) of the Code.

In Barter Business Bureau of Washington, D.C., Inc. v. United States, 326 U.S. 275, the Supreme Court held that the presence of a single non-exempt purpose, if substantial in nature, will destroy a claim for exemption regardless of the number or importance of truly exempt purposes.

Operating for the benefit of private parties constitutes a substantial nonexempt purpose. Old Dominion Box Co. v. United States, 477 F. 2d 340 (4th Cir. 1973), cert. denied 413 U.S. 910 (1973).

Leon A. Beeghly v. Commissioner, 35 T.C. 490 (1960), provided that where an exempt organization engages in a transaction with a related interest and there is a purpose to benefit the private interest rather than the organization, exemption may be lost even though the transaction ultimately proves profitable for the exempt organization.

National Association for the Legal Support of Alternative Schools, Petitioner, v. Commissioner of Internal Revenue, Respondent 71 T.C. 118; (1978) National Association was founded to promote better education for children through expanded private educational

opportunities, and to provide the public information on alternatives to public education at little or no cost. It was decided that this organization qualified for exemption based on the fact that this organization provided pertinent information to the public among its activities, and thus operated without serving primarily the private interests of its members, or those who created the organization.

In Revenue Ruling 71-395, 1971-2 C.B. 226, an organization formed and operated by a group of artists for the sole purpose of exhibiting and selling their works was denied exemption under Code section 501(c)(3). Although there was incidental benefit to the general public through viewing of artworks on public display, the Court found that the organization's primary purpose was to provide a vehicle for advancing its members' careers and promoting the sale of their artworks. This rationale was also expressed in Revenue Ruling 76-152, 1976-1 C.B. 151, wherein exemption was denied to an organization formed to promote community understanding of modern art tends by exhibiting and selling the works of local artists on a commission basis, even though the artists themselves were not involved in the operation of the gallery.

In Revenue Ruling 67-392, 1967-2 C.B. 191, an organization that aided young aspiring musicians and singers by conducting weekly workshops, sponsoring public concerts, and securing paid engagements for them was found to qualify for exemption. The organization did not charge for any of its services, and was operated by persons unrelated to the young musical artists that it aided.

Taxpayer's Position:

In a letter dated [REDACTED] it is stated that the organization is actually [REDACTED] and because [REDACTED] owns all of the musical equipment, [REDACTED] allows individual musicians and vocalists to come to [REDACTED] home and play musical compositions created by [REDACTED]

In a phone conversation with the founder on [REDACTED] [REDACTED] proposed to clarify the exempt purpose of the organization. [REDACTED] stated that the organization is furthering educational purposes by educating the musicians that come to the organization to play and that the compositions of music are of the crossover type so it will be educational to the audience as well. In addition, [REDACTED] stated that [REDACTED] applied for the aforementioned grant from the [REDACTED] and not in the name of the organization. [REDACTED] will be personally responsible for all income received and all expenses of the organization and this include the grant. [REDACTED] states that [REDACTED] is the owner of this organization and [REDACTED] will personally operate it.

In a response received [REDACTED] [REDACTED] personal goal is to produce music on a professional level, and that [REDACTED] is using the organization to do this. In addition, the founder, [REDACTED] is soliciting a grant in order for [REDACTED] group of musicians to record a compilation of songs, have these submitted to a recording

company for pressing, and have the recordings produced and distributed for sale to the general public for their mental psychological and emotional consumer consumption. This is how the organization will serve the general public.

also states that there is no substantial private benefit involved in your organization as the musicians only receive compensation for playing.

In a second response dated continues to state that the sole purpose of the organization is to form a group of individual musicians to compose, produce, and present contemporary style music to the educational benefit of those selected to play.

stated that inurement is not an issue in case, since the organization does not have any income. However, states that the organization does exist for the successful musical, business, and educational means for the founder/owner, and all musicians and vocalists associated with the organization.

states that does not have to comply with Revenue Ruling 65-271 because as a private operating foundation, no educational or public benefit needs to be present.

The response is closed by stating that the organization hopes to be beneficial to the general public by helping them to appreciate contemporary music and civilization as a whole.

In a final response dated the states that feels that may be requesting exemption from the wrong division of the Internal Revenue Service. was compelled to think that was buying exemption from Federal income tax under section 501(c)(3) of the Code with the user fee from the

The Service's Position and Conclusion:

Based upon the facts presented, we hold that your organization does not meet the requirements for tax exemption under section 501(c)(3) of the Code for the following reasons.

Your constitution does not satisfy the organizational requirements of the Regulations. You also do not satisfy the operational requirements of the Regulations.

Your purpose is to enable participate in recording music for compensation. In addition, your recordings are to be copyrighted in the and sold to the general public in a commercial manner. The collaboration of musicians to produce professional music for the ultimate benefit of who created the contemporary compositions, is not an exempt activity under section 501(c)(3) of the Code. While there may

be some benefit to some members of the public through exposure to new musical compositions or arrangements, this benefit is incidental to the benefit afforded to [REDACTED]

Your organizing document does not provide that, at dissolution, all assets will be distributed for purposes set under section 501(c)(3). The assets were [REDACTED] when [REDACTED] created the organization, will belong to [REDACTED] during the life of the organization, and if the organization were to dissolve, would continue to be in [REDACTED] possession.

[REDACTED] exercises total control over the organization. Your Constitution states that [REDACTED] is the officer of power in charge and has full and total responsibility of all financial and compensation issues. The musicians and vocalists are listed as board members, but are only compensated musicians who participate on a "play-for-pay" basis. Any and all copyrighted musical materials are of a personal nature [REDACTED] and will be placed in [REDACTED] name and not in the organization's name. Your organization's sole purpose is to produce music on a professional level [REDACTED] and to use a grant to accomplish this. [REDACTED] states that he was instructed to apply for exemption under section 501(c)(3) of the Code in order to obtain a grant from the [REDACTED]. The operation of such an organization would allow control of the net earnings of the organization to be received by one person, which constitutes inurement.

Since [REDACTED] was formed to ultimately benefit [REDACTED] and [REDACTED], this would not constitute an exempt purpose. Also, as stated earlier, the participating musicians and vocalists are also beneficiaries of this organization. [REDACTED] these individuals, this constitutes substantial private benefit as well.

In addition, private solicitation of public funds by the founder constitutes evidence of inurement. [REDACTED] has requested funds from the [REDACTED] for start-up capital for the organization. However, the grant was requested in the name of the [REDACTED]. Since there is no public representation [REDACTED] and as shown, the founder has total control over all financial transactions of [REDACTED]. Section 1.501(c)(3)-1(d)(1)(ii) of the Regulations states an organization must show that it serves a public rather than a private interest. Thus, in order for [REDACTED] to meet the requirement of this subsection, it must provide evidence that this organization is not controlled, directly or indirectly, by a private interest, or controlled by a designated individual.

By soliciting funds in this manner, with no consideration of the applicant organization, [REDACTED] appears to serve the private interest of the [REDACTED]. As in Old Dominion Box Co. v. United States, 4 F. 2d 340 (4th Cir. 1973), cert. denied 413 U.S. 910

[REDACTED]

(1973) operating for the benefit of private parties constitutes a substantial nonexempt purpose.

Like the organizations described in Revenue Rulings 71-395 and 76-152, you are providing a means for individuals to further their artistic careers and to obtain compensation for such endeavors. The fact that [REDACTED] is a primary beneficiary of your activities, and that all other participating musicians will be selected by the [REDACTED] further argues against a finding of public benefit. Unlike the organization described in Revenue Ruling 67-392, the musicians that you will aid were not selected by impartial individuals who will derive no personal benefit from aiding in the artists' careers.

Based on the facts provided, we are unable to conclude that the organization is organized and operated exclusively for public rather than private purposes. A substantial part of the organization's activities are not in furtherance of an exempt purpose, under section 501(c)(3) of the Code.

Accordingly, you do not qualify for exemption as an organization described in section 501(c)(3) of the Code.

Form 6018
(Rev. Aug. 1983)

Department of the Treasury - Internal Revenue Service
Consent to Proposed Adverse Action
(All references are to the Internal Revenue Code)

Case Number

Date of Latest Determination Letter

Employer Identification Number

Date of Proposed Advers. Action Letter

Name and Address of Organization

I consent to the proposed adverse action relative to the above organization as shown below. I understand that if Section 7428, Declaratory Judgments Relating to Status and Classification of Organizations under Section 501(c)(3), etc. applies, I have the right to protest the proposed adverse action.

NATURE OF ADVERSE ACTION

☒ Denial of exemption

☐ Revocation of exemption, effective

☐ Modification of exemption from section 501(c)() to section 501(c)(), effective

☐ Classification as a private foundation described in section 509(a), effective

☐ Classification as a private operating foundation described in sections 509(a) and 4942(j)(3), effective for

☐ Classification as an organization described in section 509(a)(), effective

☐ Classification as an organization described in section 170(b)(1)(A)(), effective

If you agree to the adverse action shown above, please sign and return this consent. You should keep a copy for your records.

If you sign this consent before you have exhausted your administrative appeal rights, you may lose your rights to a declaratory judgment under section 7428.

(Signature instructions on Back)

Name of Organization:

Signature and Title

Date

Signature and Title

Date